



U.S. AGENCY FOR
INTERNATIONAL
DEVELOPMENT

September 25, 1998

MEMORANDUM FOR **D-AA/M, Richard C. Nygard,**
Acting Chief Information Officer

M/FM, Tony Cully, Acting Chief Financial Officer

FROM: IG/A/ITSA, Theodore P. Alves *Theodore P. Alves*

SUBJECT: Audit of the Process **USAID** Used to Prepare Its Fiscal Year 1997 Financial Statements From the General Ledger (Audit Report No. A-000-98-001-F)

This is our final report on the subject audit. We reviewed your comments to our draft report and have included them in their entirety as Appendix II. The report contains no recommendations.

Thank you for the cooperation and assistance extended to our auditors during this assignment.

Background

Since fiscal year 1996, the Agency for International Development (**USAID**) has been required under the Government Management Reform Act to compile **USAID-wide** financial statements and supplemental information. These financial statements are to not only report **USAID's** financial position and results of operations, but are also to provide further information allowing Congress and the public to assess management performance and stewardship of **USAID** resources. Accordingly, **USAID** management's ability to develop and maintain adequate internal controls, accounting systems and procedures to generate reliable financial statements is critical to the success of **USAID's** annual reporting.

USAID is a decentralized organization with missions and accounting centers spread around the world. To better manage its decentralized operations **USAID** deployed the New Management System (NMS) on October 1, 1996—the start of fiscal year 1997. NMS was designed to replace aging, and ineffective computer systems used to perform accounting, budgeting, procurement, and operational functions. It was also designed to be the primary system for conducting **USAID** business, recording accounting transactions, and preparing financial and management information. Once deployed however, NMS did not operate effectively and **USAID** had to continue to rely on some of its legacy, non-integrated financial management

systems to record and process fiscal year 1997 transactions. It also had to rely on these non-integrated systems to produce data needed to prepare its fiscal year 1997 annual financial statements.

Audit Objective

In support of the Government Management Reform Act and the Office of Inspector General's audit of USAID's fiscal year 1998 financial statements, the Office of Information Technology and Special Audits conducted this audit to describe the system used by USAID to prepare its fiscal year 1997 financial statements from the general ledger. The preparation of USAID's financial statements had previously been an undefined and undocumented process. Our audit sought to define the preparation process and to identify barriers to the production of USAID's financial statements. The objective of our audit was as follows:

- **How did USAID prepare its fiscal year 1997 financial statements from the general ledger?**

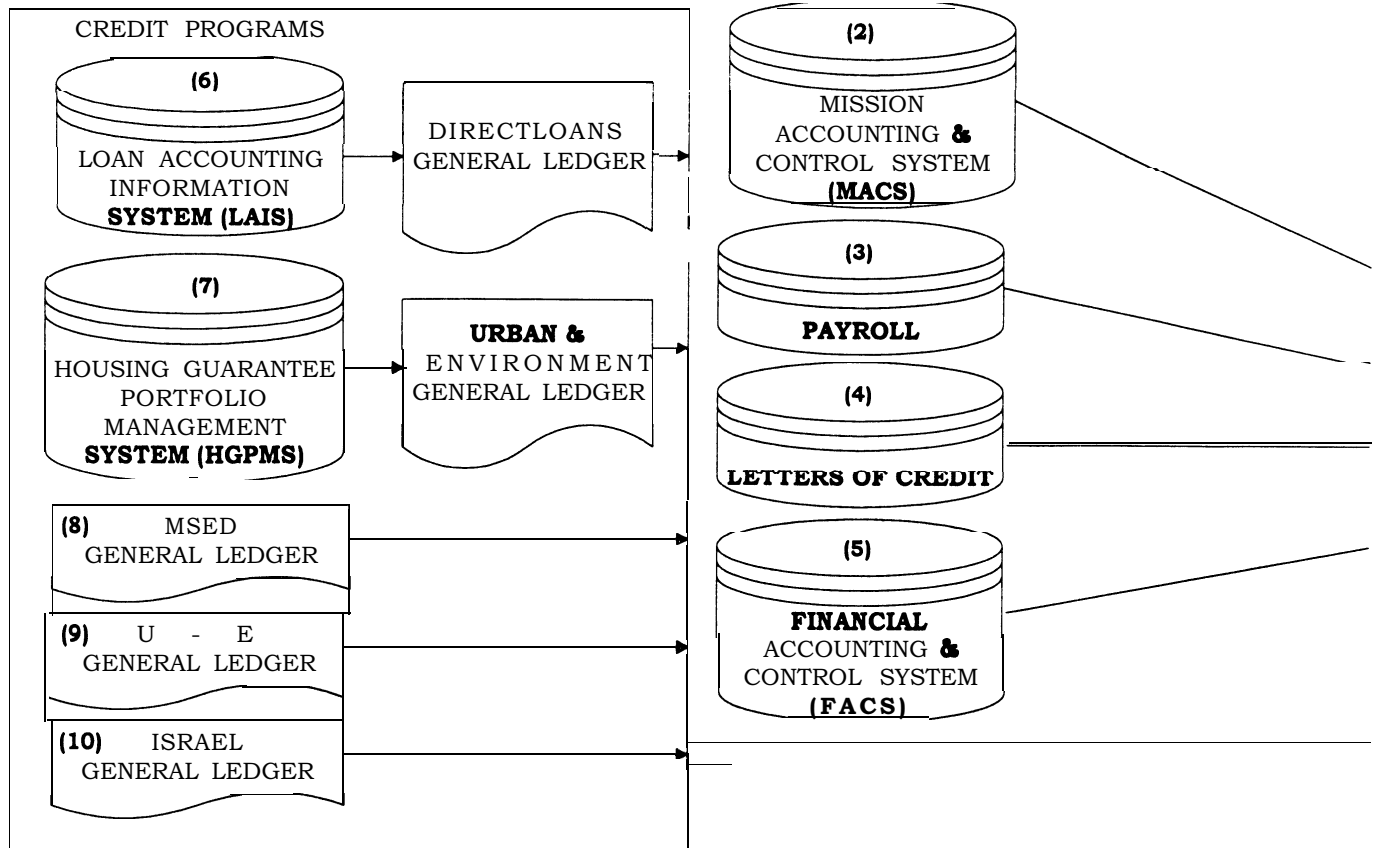
A full description of the scope and methodology is contained in Appendix I.

Process to Prepare the Financial Statements

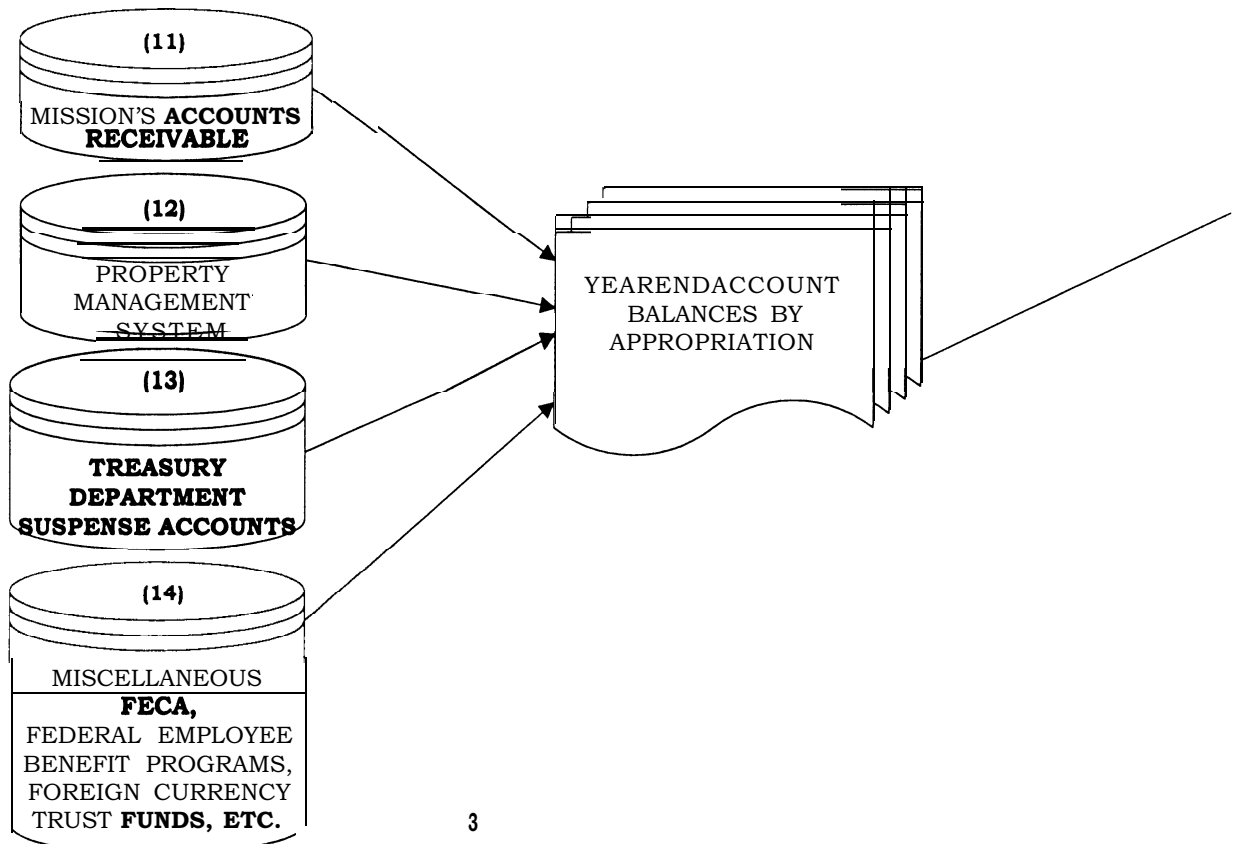
USAID prepared its fiscal year 1997 financial statements by compiling data from more than 14 principal financial management systems. Summarized account balances that were generated from these systems were manually incorporated and combined into 35 working trial balances, which summarized account balances by appropriation. Year-end adjustments were manually made to the account balances in these 35 trial balances and then the adjusted year-end account balances were summarized into 6 working trial balances by fund category. These six working trial balances were then summarized into one working consolidated statement of financial position. The summarized totals from the working consolidated statement of financial position were then reported in USAID's financial statements. The entire financial statement preparation process is outlined on pages 3 and 4.

PROCESS USED TO PREPARE USAID'S FY 97

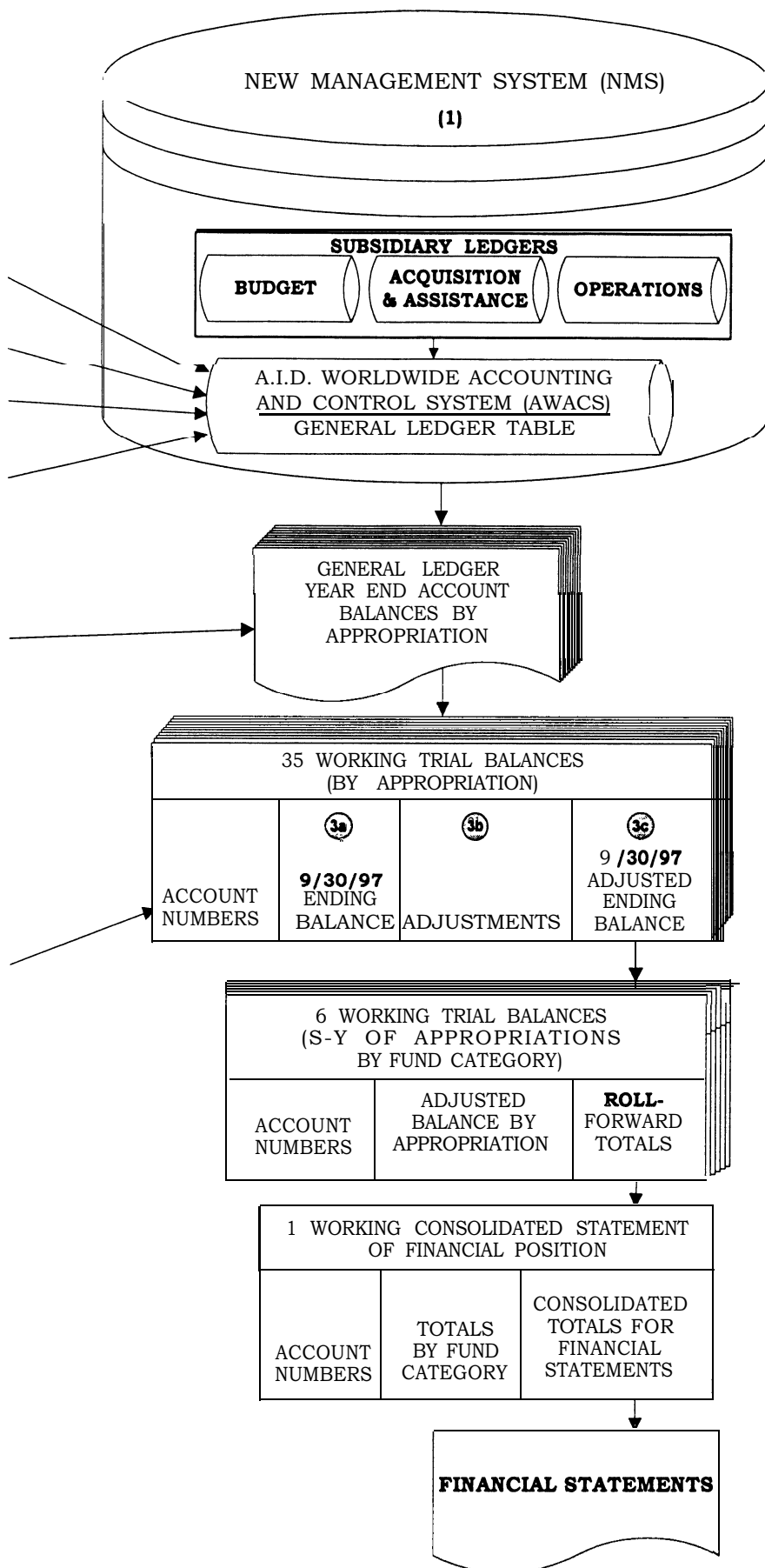
SYSTEMS OUTSIDE NMS (DATA MANUALLY POSTED TO NMS G/L)



SYSTEMS OUTSIDE NMS (DATA NOT POSTED TO NMS G/L)



FINANCIAL STATEMENTS FROM ITS GENERAL LEDGER



1 NMS (USAID'S CORE FINANCIAL MANAGEMENT SYSTEM) ELECTRONICALLY GENERATES 30 FINANCIAL REPORTS WHICH SUMMARIZE YEAR-END GENERAL LEDGER ACCOUNT BALANCES BY APPROPRIATION.

2 COPIES OF 30 GENERAL LEDGER YEAR-END ACCOUNT BALANCE REPORTS THAT ARE GENERATED BY NMS AND 5 GENERAL LEDGER REPORTS GENERATED BY SYSTEMS OPERATING OUTSIDE OF NMS (I.E. CREDIT PROGRAM SYSTEMS).

3a YEAR-END ACCOUNT BALANCES FROM STEP 2 ARE RECORDED IN 35 MANUALLY CREATED WORKING TRIAL BALANCES (BY APPROPRIATION).

3b YEAR-END ADJUSTING ENTRIES, INCLUDING ENTRIES TO RECORD LINE ITEMS NOT INCLUDED IN THE GENERAL LEDGER, ARE RECORDED IN THE WORKING TRIAL BALANCE.

3c COMPUTE THE ADJUSTED ENDING ACCOUNT BALANCES (I.E., STEP 3A + STEP 3B). ADJUSTED ENDING BALANCES ROLL FORWARD TO A SUMMARY OF APPROPRIATIONS BY FUND CATEGORY.

4 ADJUSTED ENDING BALANCES BY APPROPRIATION ARE SUMMARIZED IN 6 WORKING TRIAL BALANCES BY FUND CATEGORY AND ROLLED FORWARD TO A WORKING CONSOLIDATED STATEMENT OF FINANCIAL POSITION.

5 ACCOUNT BALANCES BY FUND CATEGORY ARE SUMMARIZED IN A WORKING CONSOLIDATED STATEMENT OF FINANCIAL POSITION AND THE CONSOLIDATED TOTALS ROLL FORWARD TO THE FINANCIAL STATEMENTS.

6 USAID'S FINANCIAL STATEMENTS

As illustrated in the flowchart, **USAID** has a variety of financial systems. Some systems are electronic (e.g. the Mission Accounting and Control System - MACS) and some are manual (e.g. Ukraine Credit Program). Further, some systems provide summary data that is manually posted to the NMS general ledger (e.g. Payroll); and some provide data which is not posted to the NMS general ledger, but is recorded in **USAID's** financial statements (e.g. Property Management System).

The Office of Financial Management's Office of Central Accounting and Reporting (CAR) is the primary office responsible for compiling data from **USAID's** financial systems and preparing **USAID's** annual financial statements. With the assistance of a public accounting firm, CAR prepared **USAID's** fiscal year 1997 financial statements by performing the six following steps:

- (1) Electronically generated using NMS (**USAID's** Core Financial Management System), 30 financial reports which summarized Sept. 30, 1997 annual account balances by appropriation (i.e. reports which summarized together 1995, 1996, and 1997 account balances for the same appropriation). For example, **USAID** receives an appropriation for operating expenses in 1995, another appropriation in 1996, and another one in 1997. The NMS-generated reports would summarize the account balances for 1995, 1996, and 1997 for the same appropriation.
- (2) Printed out copies of (a) the 30 MS-generated year-end general ledger account balance reports from step 1, and (b) 5 general ledger reports generated by systems outside of NMS showing the year-end account balances for **USAID's** 5 Credit Programs.
- (3) Recorded year-end balances from step 2 and any necessary adjusting journal entries into 35 manually-prepared working trial balances and then computed the adjusted year-end account balances. These steps are discussed in more detail below.
 - (3a) Recorded **USAID's** year-end account balances by appropriation from the financial reports in step 2 into 35 manually-prepared working trial balances. The 35 trial balances were prepared so that financial data from systems operating outside of NMS could be recorded and consolidated with data that had already been entered into **USAID's** general ledger via NMS. The 35 trial balances also served to calculate **USAID's** account balances by appropriation, which **USAID** is required to transmit annually to the Financial Management Service of the Department of Treasury via Treasury's Federal Agencies' Centralized Trial Balance System (FACTS) on the Government's On-Line Accounting Link System (GOALS). Treasury uses these balances to prepare the overall federal government's financial statements.
 - (3b) Determined the types of year-end adjusting entries that needed to be made to account balances and then recorded them in the appropriate working trial balance. Adjusting journal entries were made for a variety of reasons including: (a) to

correct data entry errors that had been made during the year, (b) to record paid, but unrecorded expenses, and (c) to record data which is not tracked by USAID's general ledger, but which is required to be reported in the financial statements (e.g. Property, Plant, & Equipment).

A total of 275 adjusting entries were made to the year-end account balances that were listed in the reports generated in step 2. In order to better understand the types of adjustments that were being made, we grouped the adjusting entries into the following general categories:

- 40 percent were made to reclassify account balances from Intragovernmental to Governmental and vice versa (*to correct manual entry errors*),
- 32 percent were related to AID Worldwide Accounting and Control System vouchers (*to record **unrecorded** A WACS vouchers*),
- 9 percent were to record line items not tracked by the NMS general ledger,
- 5 percent were to record Dept. of Treasury's Suspense Account Balances in the general ledger as USAID reports Treasury's balance instead of its own ,
- 4 percent were accruals,
- 3 percent Closing entries,
- 3 percent Other miscellaneous reclassification errors,
- 2 percent Payroll (*to record unrecorded pay **periods** and payroll accruals*), and
- 2 percent Miscellaneous.

- (3c) Calculated adjusted year-end account balances by totaling the initial NMS year-end balances from step 3a with the adjusting journal entry amounts from step 3b and recorded the adjusted ending account balances in the 35 working trial balances.
- (4) Combined and summarized the adjusted ending account balances from the 35 trial balances into 6 fund categories: Credit Program, Operating Expenses, Program Funds, Other Funds, Revolving Funds, and Trust Funds. Prepared 6 working trial balances to record the summarized balances.
- (5) Combined and summarized the account balances from the six trial balances in step 4 into one working consolidated statement of financial position.
- (6) Reported the summarized account totals from the working consolidated statement of financial position into USAID's fiscal year 1997 financial statements (i.e. Consolidated Statement of Financial Position as of September 30, 1997 and Consolidated Statement of Operations and Changes in Net Position for the Year Ended September 30, 1997).

To understand how USAID prepared its fiscal year 1997 financial statements, we traced two line items from the financial statements to their supporting general ledger balances. The two

line items included “Fund Balance with Treasury,” which totaled \$9.7 billion and “Accounts Payable-Governmental Liabilities,” which totaled \$1.7 billion. During our tracing of the two line items, we found that the working papers—which documented how USAID prepared its fiscal year 1997 financial statement—were adequate, well-organized, and easy to follow. However, we found that USAID’s lack of a single, integrated financial management system—a system required by OMB Circular No. A-127—created barriers which hindered USAID’s production of timely and reliable financial statements.

Barriers to the Production of USAID’s Financial Statements

There are several barriers which USAID has to overcome in order to produce annual financial statements. For example, USAID (1) must manually prepare its financial statements using a labor-intensive process, (2) must enter similar accounting data into multiple systems, (3) has a general ledger that does not include all financial activity, and (4) does not have the ability to query financial statement information at the transaction level. These four barriers, each of which can be linked to USAID’s lack of a single, integrated financial management system, are discussed below.

- USAID’s financial statements must be prepared manually because USAID’s financial management systems are not integrated. The compilation process involves the manual creation of 35 working trial balances that are based on (a) financial data taken from NMS-generated reports, and (b) financial data taken from systems outside of NMS. The process is labor-intensive and increases the risk of errors in the financial statements. The manual process could be eliminated if USAID had a single, automated financial management system which could electronically summarize USAID’s annual appropriations and generate account balances which must be reported annually to the Department of Treasury in an annual 2108 report (Year End Closing Statement). Such a system is required by OMB Circular No. A- 127.
- Similar financial data must be manually entered into multiple financial management systems. For example, at the transaction level mission personnel will enter an expense into MACS (*1st transaction entry*). The mission will then prepare and send a monthly summary report of MACS transactions (i.e. a U101 report) to USAID/Washington. USAID/Washington will then enter these MACS summary amounts into NMS (*2nd transaction entry*). In preparation of the annual financial statements, CAR has NMS generate reports which summarize annual appropriation balances. These summarized balances are then manually entered into a working trial balance (*3rd transaction entry*), which later rolls up into USAID’s financial statements. Such duplicate and triplicate entries are inefficient and increase the likelihood of data entry errors and inaccurate financial statement balances. OMB Circular No. A-127 states that financial system designs shall eliminate unnecessary duplication of transaction entry and that wherever appropriate, data needed by the systems to support financial functions shall be entered only once and other parts of the system shall be updated through electronic means.

- Nine percent (24 of 275) of the fiscal year 1997 adjusting journal entries were made to record account balances in the financial statements because **USAID** does not have a general ledger that includes all financial activity. For example, Property, Plant, & Equipment is a financial statement line item, but its balances were not recorded in or tracked by any of **USAID**'s general ledgers. Accordingly, year-end account balances for this line item had to be determined by request-for-data calls to missions and had to be manually added to the financial statements via year-end adjusting journal entries.

General ledger management is the central function of a core financial system. OMB Circular No. A- 127 states that financial management systems must comply with the U.S. Government Standard General Ledger at the transaction level. Joint Financial Management Improvement Program requirements add that all transactions to record financial events must post, either individually or in summary, to the general ledger, regardless of the origin of the transactions. Accordingly, a single, integrated financial management system with a complete and fully operational general ledger would eliminate the need to record account balances, which are not tracked by the NMS general ledger, to the financial statements.

- Financial statement and NMS general ledger information cannot be electronically queried at the transaction level. To illustrate, since **USAID**'s financial statements are prepared manually with summary information, data reported in the statements cannot be electronically queried at the financial statement, fund category, appropriation, or transaction levels. Further, since summarized data-not transaction data-from non-NMS systems is recorded in the NMS general ledger, details of the data cannot be queried by NMS. Detailed queries at the financial statement and NMS levels would allow **USAID** managers to better analyze **USAID**'s financial situation and could lead to improvements in **USAID**'s programs.

The Joint Financial Management Improvement Program requires a core financial system which can be queried to present specific detailed data as requested and which allows users to design reports and extract files for their specific requirements. OMB Circular A-1 27 requires data to be entered into the Standard General Ledger at the transaction level. Accordingly, a single, integrated **financial** management system which allowed financial data to be queried from different angles would be beneficial to **USAID** managers and facilitate the development of the financial statements.

In conclusion, there are several barriers which **USAID** has in producing its financial statements. We are not making any formal recommendations because **USAID** reported the lack of an effective, integrated **financial** management system as a material weakness in its fiscal year 1997 Federal Managers' Financial Integrity Act report and because **USAID** is taking action to address the weakness. **USAID** is in the process of evaluating new financial management systems and the need to correct the weaknesses described in this report should be considered during the evaluation process to ensure that a new system electronically produces timely and accurate **financial** statements and eliminates or minimizes current barriers to

USAID's financial reporting requirements. However, until a single, integrated financial management system is adopted by USAID, poor policy decisions are more likely to be made due to inaccurate or untimely information; managers are less likely to be able to report accurately to Congress; and scarce resources are more likely to be directed toward the collection of information rather than to the delivery of the intended programs.

Management Comments and **Our** Evaluation

USAID's Acting Chief Financial Officer stated that he found the flowchart on the process used to prepare the fiscal year 1997 Financial Statements informative and he agreed, for the most part, with the audit report's findings. However, he stated that the last sentence of the audit report seemed to overstate the consequences of not having a single, integrated financial management system and stated that he thought that it would be unrealistic to believe that financial reports would be the only basis for decisions made by managers and legislators.

We agree that reports generated from systems maintained by the Office of Financial Management (FM) may not be the only basis for decisions made by managers and legislators. In fact, it is precisely because many USAID managers rely on cuff records and other financial systems-not integrated with the core financial management system-to manage USAID operations, that we disagree with your conclusion that this report overstates the consequences of not having a single, integrated financial management system.

OMB Circular A- 127 and the Joint Financial Management Improvement Program require agencies to establish and maintain an integrated financial management system so they can efficiently track and summarize financial information and so managers, who are making daily decisions about the allocation of resources, can have access to timely and accurate financial information as a basis for their decisions. Without timely and accurate financial information, poor policy decisions are more likely to be made and reporting, both internal and external, is more likely to be inconsistent and inaccurate. Single, integrated financial management systems can provide complete, consistent, timely, and accurate financial information and accordingly, we do not believe that we have overstated the consequences of not having such a system.

The Acting Chief Financial Officer also stated in his comments that he was concerned with the report's use of the phrase "a single, integrated financial management system" and pointed out that per OMB Circular A-127 an integrated system does not mean having only one system. Further, he stated that if USAID procures and implements a new core accounting system, the new system will not be the only system comprising the integrated financial management system. We agree with USAID's interpretation of OMB Circular A-127's definition of an integrated financial management system and we support USAID's efforts to integrate the core financial management system with the rest of USAID's financial management systems.

SCOPE AND METHODOLOGY

Scope

Our audit of how **USAID** prepared its fiscal year 1997 financial statements covered the development of **USAID's** Consolidated Statement of Financial Position and its Consolidated Statement of Operations and Changes in Net Position. The audit also covered the flow of data from year-end general ledger account balances to the financial statements, but we did not audit the general ledger balances. We also did not audit how **USAID** prepared (1) the overview section of its financial statements, (2) the footnotes to the **financial** statements, or (3) the performance results reported in the financial statements.

Our audit was conducted from July **29**, 1998 to August **21**, 1998 in accordance with generally accepted government auditing standards. Audit fieldwork was primarily conducted in the Office of Financial Management's Office of Central Accounting and Reporting at **USAID/Washington**.

We did not aim to determine whether **USAID** had properly prepared its fiscal year 1997 **financial** statements as the Office of Inspector General had already disclaimed an opinion on the statements (See Audit Report No. 0-000-98-001-F). However, the audit did aim to describe and outline the procedures **USAID** followed to develop the financial statements.

Methodology

To determine how **USAID** developed its financial statements, we held discussions with Financial Management officials and traced two financial statement line items from the financial statements to the supporting general ledger balances that were listed in the New Management System. We were requested to trace the two line items, Fund Balance with Treasury totaling \$9.7 billion and Accounts Payable-Governmental Liabilities totaling \$1.7 billion, by the Office of Financial Audits, which had selected the line items based on their materiality to the fiscal year 1997 financial statements. We then worked backward from the **financial** statements to determine what amounts had been included in the totals reported on the financial statements.

We began by tracing the line items from the financial statements to a Consolidated Statement of Financial Position. Balances listed on the Consolidated Statement of Financial Position were then traced to supporting Working Trial Balances by Fund Category. Account balances from the Working Trial Balances by Fund Category were then traced to supporting Working Trial Balances by Appropriation, which listed year-end general ledger account balances, year-end adjusting journal entries, and the adjusted ending account balances.

To test the year-end balances that were recorded in the Working Trial Balances by Appropriation, we traced amounts recorded on the trial balances to those listed on NMS-generated financial reports. To test adjustments that were made to the year-end general ledger account balances, we judgementally selected and traced to the supporting adjusting journal entries, all adjusting journal entries which were made to the accounts Fund Balance with Treasury and Accounts Payable-Governmental Liabilities as recorded in 4 of the 35 Working Trial Balances by Appropriation.



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September 25, 1998

MEMORANDUM

TO: IG/A/ISTA, Theodore Alves
FROM: M/FM, Tony Gully, Acting CFO
SUBJECT: Audit of the Process USAID Used to Prepare Its Fiscal
Year 1997 Financial Stat-to From the General Ledger
(Draft Audit Report No. A-000-98-xxx-P)

Thank you for the opportunity to comments on the subject draft report. I found it to be most informative, in particular the flow chart on the process used to prepare the FY 1997 Financial Statements. The report will help readers understand the extraordinary effort put forth by the FM staff in preparing the FY 1997 Consolidated Financial Statements.

While I agree with the report findings for the most part, I must state that I find the consequences of not having a single, integrated financial management system to be somewhat overstated in the final sentence of the report. All of us in the federal government financial management business would hope that our reports are used as the basis for managers and legislators decisions. However, I think it would be unrealistic to believe they would be the only basis. In fact, I would guess that more often factors other than financial matters influence their decisions.

Finally, I am concerned that your definition of a single integrated financial management system may not agree with my definition.

OMB Circular A-127 defines an integrated system as:

"... a unified set of financial systems and the financial portions of mixed systems encompassing the software, hardware, personnel, processes (manual and automated), procedures, controls and data necessary to carry out financial management functions, manage financial operations of the agency and report on the agency's financial status to central agencies, Congress and the public."

It is important to note that integrated does not mean only one system. In fact, if the Agency decides to procure and implement a COTS system, for core accounting, it will not be the only system comprising the integrated financial management system. However, as suggested in the draft report, we plan to consider system which will minimize the so called "barriers" identified by the auditors.

Please contact me if you wish to discuss any portions of this response and again thank you for this report that provides positive aspects to your review of USAID's financial systems.